

Internal Revenue Service, Treasury

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Example 2. Assume the facts are the same as in example (1) except that the district director, upon examining X's income tax return, asserts an income tax deficiency of \$4, based on an asserted increase of \$10 in real estate investment trust taxable income, and no agreement is entered into between the parties. X pays the \$4 on June 1, 1979, and files suit for refund in the United States District Court. The District Court, in a decision which becomes final on November 1, 1980, holds that X did fail to report \$10 of real estate investment trust taxable income and is not entitled to any refund. (No other item of income or deduction is in issue.) X pays a dividend of \$10 on November 10, 1980, files a claim for a deficiency dividend deduction of this \$10 on November 15, 1980, and is allowed a deficiency dividend deduction of \$10 for 1977. Assume further that \$4 is refunded to X on December 31, 1980, as the result of the \$10 deficiency dividend deduction being allowed. Also assume that any assessable penalties, additional amounts, and additions to tax (including the penalty imposed by section 6697) for which X is liable are paid within 10 days of notice and demand, so that no interest is imposed on such penalties, etc. X's liability for interest for the period March 15, 1978, to June 1, 1979, is determined with respect to \$10 (the amount of the deficiency dividend deduction allowed). X's liability for interest for the period June 1, 1979, to November 15, 1980, is determined with respect to \$6, *i.e.*, \$10 minus the \$4 payment. X is entitled to interest on the \$4 overpayment for the period described in section 6611(b)(2), beginning on November 15, 1980.

(Sec. 7805, 68A Stat. 917; 26 U.S.C. 7805; sec. 860(e) (92 Stat. 2849, 26 U.S.C. 860(e)); sec. 860(g) (92 Stat. 2850, 26 U.S.C. 860(g)))

[T.D. 7936, 49 FR 2108, Jan. 18, 1984]

§ 1.860-4 Claim for credit or refund.

If the allowance of a deduction for a deficiency dividend results in an overpayment of tax, the taxpayer, in order to secure credit or refund of the overpayment, must file a claim on Form 1120X in addition to the claim for the deficiency dividend deduction required under section 860(g). The credit or refund will be allowed as if on the date of the determination (as defined in section 860(e)) two years remained before the expiration of the period of limitations on the filing of claim for refund

for the taxable year to which the overpayment relates.

(The reporting requirements of this section were approved by the Office of Management and Budget under control number 1545-0045)

(Sec. 7805, 68A Stat. 917; 26 U.S.C. 7805; sec. 860(e) (92 Stat. 2849, 26 U.S.C. 860(e)); sec. 860(g) (92 Stat. 2850, 26 U.S.C. 860(g)))

[T.D. 7936, 49 FR 2109, Jan. 18, 1984]

§ 1.860-5 Effective date.

(a) *In general.* Section 860 and §§ 1.860-1 through 1.860-4 apply with respect to determinations after November 6, 1978.

(b) *Prior determination of real estate investments trusts.* Section 859 (as in effect before the enactment of the Revenue Act of 1978) applies to determinations with respect to real estate investment trusts occurring after October 4, 1976, and before November 7, 1978. In the case of such a determination, the rules in §§ 1.860-1 through 1.860-4 apply, a reference in this chapter 1 to section 860 (or to a particular provision of section 860) shall be considered to be a reference to section 859 (or to the corresponding substantive provision of section 859), as in effect before enactment of the Revenue Act of 1978, and "qualified investment entity" in §§ 1.381(c)25-1(a) and 1.860-1 through 1.860-3 means a real estate investment trust.

(Sec. 7805, 68A Stat. 917; 26 U.S.C. 7805; sec. 860(e) (92 Stat. 2849, 26 U.S.C. 860(e)); sec. 860(g) (92 Stat. 2850, 26 U.S.C. 860(g)))

[T.D. 7936, 49 FR 2109, Jan. 18, 1984]

§ 1.860A-0 Outline of REMIC provisions.

This section lists the paragraphs contained in §§ 1.860A-1 through 1.860G-3.

Section 1.860A-1 Effective dates and transition rules.

- (a) In general.
- (b) Exceptions.
 - (1) Reporting regulations.
 - (2) Tax avoidance rules.
 - (i) Transfers of certain residual interests.
 - (ii) Transfers to foreign holders.
 - (iii) Residual interests that lack significant value.
 - (3) Excise taxes.
 - (4) Rate based on current interest rate.
 - (i) In general.
 - (ii) Rate based on index.
 - (iii) Transition obligations.

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(5) Accounting for REMIC net income of foreign persons.

§ 1.860C-2 Determination of REMIC taxable income or net loss.

- (a) Treatment of gain or loss.
- (b) Deductions allowable to a REMIC.
 - (1) In general.
 - (2) Deduction allowable under section 163.
 - (3) Deduction allowable under section 166.
 - (4) Deduction allowable under section 212.
 - (5) Expenses and interest relating to tax-exempt income.

§ 1.860D-1 Definition of a REMIC.

- (a) In general.
- (b) Specific requirements.
 - (i) Interests in a REMIC.
 - (i) In general.
 - (ii) De minimis interests.
 - (2) Certain rights not treated as interests.
 - (i) Payments for services.
 - (ii) Stripped interests.
 - (iii) Reimbursement rights under credit enhancement contracts.
 - (iv) Rights to acquire mortgages.
 - (3) Asset test.
 - (i) In general.
 - (ii) Safe harbor.
 - (4) Arrangements test.
 - (5) Reasonable arrangements.
 - (i) Arrangements to prevent disqualified organizations from holding residual interests.
 - (ii) Arrangements to ensure that information will be provided.
 - (6) Calendar year requirement.
 - (c) Segregated pool of assets.
 - (1) Formation of REMIC.
 - (2) Identification of assets.
 - (3) Qualified entity defined.
 - (4) Election to be treated as a real estate mortgage investment conduit.
 - (1) In general.
 - (2) Information required to be reported in the REMIC's first taxable year.
 - (3) Requirement to keep sufficient records.

§ 1.860E-1 Treatment of taxable income of a residual interest holder in excess of daily accruals.

- (a) Excess inclusion cannot be offset by otherwise allowable deductions.
 - (1) In general.
 - (2) Affiliated groups.
 - (3) Special rule for certain financial institutions.
 - (i) In general.
 - (ii) Ordering rule.
 - (A) In general.
 - (B) Example.
 - (iii) Significant value.
 - (iv) Determining anticipated weighted average life.
 - (A) Anticipated weighted average life of the REMIC.

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(B) Regular interests that have a specified principal amount.

(C) Regular interests that have no specified principal amount or that have only a nominal principal amount, and all residual interests.

(D) Anticipated payments.

- (b) Treatment of a residual interest held by REITs, RICs, common trust funds, and subchapter T cooperatives. [Reserved]

(c) Transfers of noneconomic residual interests.

- (1) In general.
- (2) Noneconomic residual interest.
- (3) Computations.
- (4) Safe harbor for establishing lack of improper knowledge.
- (5) Asset test.
- (6) Definitions for asset test.
- (7) Formula test.
- (8) Conditions and limitations on formula test.
- (9) Examples.
- (10) Effective dates.
- (d) Transfers to foreign persons.

§ 1.860E-2 Tax on transfers of residual interest to certain organizations.

- (a) Transfers to disqualified organizations.
 - (1) Payment of tax.
 - (2) Transitory ownership.
 - (3) Anticipated excess inclusions.
 - (4) Present value computation.
 - (5) Obligation of REMIC to furnish information.
 - (6) Agent.
 - (7) Relief from liability.
- (i) Transferee furnishes information under penalties of perjury.
 - (ii) Amount required to be paid.
 - (b) Tax on pass-thru entities.
 - (1) Tax on excess inclusions.
 - (2) Record holder furnishes information under penalties of perjury.
 - (3) Deductibility of tax.
 - (4) Allocation of tax.

§ 1.860F-1 Qualified liquidations.

§ 1.860F-2 Transfers to a REMIC.

- (a) Formation of a REMIC.
 - (1) In general.
 - (2) Tiered arrangements.
 - (i) Two or more REMICs formed pursuant to a single set of organizational documents.
 - (ii) A REMIC and one or more investment trusts formed pursuant to a single set of documents.
 - (b) Treatment of sponsor.
 - (1) Sponsor defined.
 - (2) Nonrecognition of gain or loss.
 - (3) Basis of contributed assets allocated among interests.
 - (i) In general.
 - (ii) Organizational expenses.
 - (A) Organizational expense defined.
 - (B) Syndication expenses.

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- (iii) Pricing date.
- (4) Treatment of unrecognized gain or loss.
- (i) Unrecognized gain on regular interests.
- (ii) Unrecognized loss on regular interests.
- (iii) Unrecognized gain on residual interests.
- (iv) Unrecognized loss on residual interests.
- (5) Additions to or reductions of the sponsor's basis.
- (6) Transferred basis property.
- (c) REMIC's basis in contributed assets.

§ 1.860F-4 REMIC reporting requirements and other administrative rules.

- (a) In general.
- (b) REMIC tax return.
- (1) In general.
- (2) Income tax return.
- (c) Signing of REMIC return.
- (1) In general.
- (2) REMIC whose startup day is before November 10, 1988.
- (i) In general.
- (ii) Startup day.
- (iii) Exception.
- (d) Designation of tax matters person.
- (e) Notice to holders of residual interests.
- (1) Information required.
- (i) In general.
- (ii) Information with respect to REMIC assets.
- (A) 95 percent asset test.
- (B) Additional information required if the 95 percent test not met.
- (C) For calendar quarters in 1987.
- (D) For calendar quarters in 1988 and 1989.
- (iii) Special provisions.
- (2) Quarterly notice required.
- (i) In general.
- (ii) Special rule for 1987.
- (3) Nominee reporting.
- (i) In general.
- (ii) Time for furnishing statement.
- (4) Reports to the Internal Revenue Service.
- (f) Information returns for persons engaged in a trade or business.

§ 1.860G-1 Definition of regular and residual interests.

- (a) Regular interest.
- (1) Designation as a regular interest.
- (2) Specified portion of the interest payments on qualified mortgages.
- (i) In general.
- (ii) Specified portion cannot vary.
- (iii) Defaulted or delinquent mortgages.
- (iv) No minimum specified principal amount is required.
- (v) Specified portion includes portion of interest payable on regular interest.
- (vi) Examples.
- (3) Variable rate.
- (i) Rate based on current interest rate.
- (ii) Weighted average rate.

- (A) In general.
- (B) Reduction in underlying rate.
- (iii) Additions, subtractions, and multiplications.
- (iv) Caps and floors.
- (v) Funds-available caps.
- (A) In general.
- (B) Facts and circumstances test.
- (C) Examples.
- (vi) Combination of rates.
- (4) Fixed terms on the startup day.
- (5) Contingencies prohibited.
- (b) Special rules for regular interests.
- (1) Call premium.
- (2) Customary prepayment penalties received with respect to qualified mortgages.
- (3) Certain contingencies disregarded.
- (i) Prepayments, income, and expenses.
- (ii) Credit losses.
- (iii) Subordinated interests.
- (iv) Deferral of interest.
- (v) Prepayment interest shortfalls.
- (vi) Remote and incidental contingencies.
- (4) Form of regular interest.
- (5) Interest disproportionate to principal.
- (i) In general.
- (ii) Exception.
- (6) Regular interest treated as a debt instrument for all Federal income tax purposes.
- (c) Residual interest.
- (d) Issue price of regular and residual interests.
- (1) In general.
- (2) The public.

§ 1.860G-2 Other rules.

- (a) Obligations principally secured by an interest in real property.
- (1) Tests for determining whether an obligation is principally secured.
- (i) The 80-percent test.
- (ii) Alternative test.
- (2) Treatment of liens.
- (3) Safe harbor.
- (i) Reasonable belief that an obligation is principally secured.
- (ii) Basis for reasonable belief.
- (iii) Later discovery that an obligation is not principally secured.
- (4) Interests in real property; real property.
- (5) Obligations secured by an interest in real property.
- (6) Obligations secured by other obligations; residual interests.
- (7) Certain instruments that call for contingent payments are obligations.
- (8) Release of a lien on an interest in real property securing a qualified mortgage; defeasance.
- (9) Stripped bonds and coupons.
- (b) Assumptions and modifications.
- (1) Significant modifications are treated as exchanges of obligations.
- (2) Significant modification defined.
- (3) Exceptions.

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- (4) Modifications that are not significant modifications.
- (5) Assumption defined.
- (6) Pass-thru certificates.
- (7) Test for determining whether an obligation continues to be principally secured following certain types of modifications.
- (c) Treatment of certain credit enhancement contracts.
 - (1) In general.
 - (2) Credit enhancement contracts.
 - (3) Arrangements to make certain advances.
 - (i) Advances of delinquent principal and interest.
 - (ii) Advances of taxes, insurance payments, and expenses.
 - (iii) Advances to ease REMIC administration.
 - (4) Deferred payment under a guarantee arrangement.
 - (d) Treatment of certain purchase agreements with respect to convertible mortgages.
 - (1) In general.
 - (2) Treatment of amounts received under purchase agreements.
 - (3) Purchase agreement.
 - (4) Default by the person obligated to purchase a convertible mortgage.
 - (5) Convertible mortgage.
 - (e) Prepayment interest shortfalls.
 - (f) Defective obligations.
 - (1) Defective obligation defined.
 - (2) Effect of discovery of defect.
 - (g) Permitted investments.
 - (1) Cash flow investment.
 - (i) In general.
 - (ii) Payments received on qualified mortgages.
 - (iii) Temporary period.
 - (2) Qualified reserve funds.
 - (3) Qualified reserve asset.
 - (i) In general.
 - (ii) Reasonably required reserve.
 - (A) In general.
 - (B) Presumption that a reserve is reasonably required.
 - (C) Presumption may be rebutted.
 - (h) Outside reserve funds.
 - (i) Contractual rights coupled with regular interests in tiered arrangements.
 - (1) In general.
 - (2) Example.
 - (j) Clean-up call.
 - (1) In general.
 - (2) Interest rate changes.
 - (3) Safe harbor.
 - (k) Startup day.

§ 1.860G-3 Treatment of foreign persons.

- (a) Transfer of a residual interest with tax avoidance potential.
 - (1) In general.
 - (2) Tax avoidance potential.
 - (i) Defined.
 - (ii) Safe harbor.

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- (3) Effectively connected income.
- (4) Transfer by a foreign holder.
- (b) Accounting for REMIC net income
 - (1) Allocation of partnership income to a foreign partner.
 - (2) Excess inclusion income allocated by certain pass-through entities to a foreign person.

[T.D. 8458, 57 FR 61299, Dec. 24, 1992; 58 FR 15089, Mar. 19, 1993, as amended by T.D. 8614, 60 FR 42787, Aug. 17, 1995; T.D. 9004, 67 FR 47453, July 19, 2002; T.D. 9128, 69 FR 26041, May 11, 2004; T.D. 9272, 71 FR 43365, Aug. 1, 2006; T.D. 9415, 73 FR 40172, July 14, 2008; T.D. 9463, 74 FR 47438, Sept. 16, 2009]

§ 1.860A-1 Effective dates and transition rules.

(a) *In general.* Except as otherwise provided in paragraph (b) of this section, the regulations under sections 860A through 860G are effective only for a qualified entity (as defined in § 1.860D-1(c)(3)) whose startup day (as defined in section 860G(a)(9) and § 1.860G-2(k)) is on or after November 12, 1991.

(b) *Exceptions—*(1) *Reporting regulations.*(i) Sections 1.860D-1(c) (1) and (3), and § 1.860D-1(d) (1) through (3) are effective after December 31, 1986.

(ii) Sections 1.860F-4 (a) through (e) are effective after December 31, 1986 and are applicable after that date except as follows:

(A) Section 1.860F-4(c)(1) is effective for REMICs with a startup day on or after November 10, 1988.

(B) Sections 1.860F-4(e)(1)(ii) (A) and (B) are effective for calendar quarters and calendar years beginning after December 31, 1988.

(C) Section 1.860F-4(e)(1)(ii)(C) is effective for calendar quarters and calendar years beginning after December 31, 1986 and ending before January 1, 1988.

(D) Section 1.860F-4(e)(1)(ii)(D) is effective for calendar quarters and calendar years beginning after December 31, 1987 and ending before January 1, 1990.

(2) *Tax avoidance rules—*(i) *Transfers of certain residual interests.* Section 1.860E-1(c) (concerning transfers of noneconomic residual interests) and § 1.860G-3(a)(4) (concerning transfers by a foreign holder to a United States person) are effective for transfers of residual interests on or after September 27, 1991.